above, there is no reason to believe that the merger would make it less profitable for the merged company than for the separate companies to pursue residential and small business customers. Indeed, the contrary is true, since, as explained above, the merged company will need residential customers to fill its expanded network in off-peak hours, and a company offering long-distance, Internet and international services to residential customers must offer local services as well in order to satisfy the demand for full-service packages.

GTE's final alternate scenario is that the merged company "may simply terminate planned investments." *GTE Comments* at 90. This apparently refers to the possibility that the merged company might be able to scale back investments MCI otherwise would have made to provide local service to areas covered by existing or planned WorldCom networks -- a cutback GTE labels as "reduced investment and less robust competition." *GTE Comments* at 97-98. But the parties are planning to expand local service and local networks; if the merged company can achieve the same amount of expansion in customer coverage with less investment, that is a real economic savings. And, as previously noted, when two competitors with less than 1% of the market merge, there is simply no anticompetitive effect.

4. The merged company will promote market-opening public policies

As part of the Commission's merger analysis, the Commission also reviews the effect of the proposed merger on "dynamic market performance," which includes, among other things, the effect the merger might have on the regulatory process of opening markets to competition. MCI and WorldCom have consistently argued in this proceeding that grant of our Application will have the effect of creating the strongest new entrant with the most at stake in the fight to open competitive markets. In fact, that is why we noted in our Joint Reply, that GTE and several Bell companies were opposing the merger – in recognition of the challenge that MCI WorldCom presents to their ability to dominate not just the local competitive arena, but the public policy one as well.

5. Barriers to entry or expansion

While the Commission in *Bell Atlantic/NYNEX* evaluated the extent to which a merger of two incumbent monopolists would discourage potential entry and expansion, there are no similar concerns presented by the merger of MCI and WorldCom. In fact, the opposite is true – the merger of these two carriers will produce a substantially beneficial effect on those carriers who are seeking to enter local markets because MCI WorldCom will have the ability to pave the way.

In the Applicants' view, the Commission should examine the effect of this merger on the ability to reduce barriers to entry and expansion into local markets. GTE's analysis, which otherwise sticks closely to the four-factor competitive format of *Bell Atlantic/NYNEX* and *BT/MCI*, conspicuously leaves out the "barriers to entry or expansion" category in discussing local markets. The reason is obvious: these barriers are enormous, and GTE has been one of the leaders in attempting to maintain them. Barriers to entry include: (1) the necessity either to build a new local network or to surmount the multiple obstacles that the incumbents have placed to utilization of their own networks for resale or unbundled network elements despite the requirements of the 1996 Act and this Commission's pro-competitive decisions; (2) the need for a recognized brand name; (3) building access; and (4) state and local regulation favoring incumbents. MCI WorldCom, with the most extensive facilities of any new entrant, MCI's brand, and the ability to undertake the investment necessary to enter local markets profitably, is best positioned to overcome these multiple barriers.

6. Potential Competition Doctrine and Measurement of Market Concentration

In the *Bell Atlantic/NYNEX* decision, the Commission noted that the potential competition doctrine should be applied to the facts of the case because there existed "evidence of potential harm to competition."[21] In the present case, applicants submit that there is no such evidence for local markets. Therefore, no analysis of the potential competition doctrine is required. The HHI indexes discussed in this record demonstrate that this merger is not likely to create or enhance market power or its exercise. On this subject, there can be no serious dispute.

D. Other competitive effects

Applicants previously demonstrated the significant cost savings and efficiencies that will result from the merger.[22] Other cost savings are further explained in the Affidavit of Sunit Patel, WorldCom's Treasurer, at Attachment B. These efficiencies will enhance the combined company's ability to raise capital, and will give it greater financial strength. To summarize, we noted that the merger will reduce our access costs because we can combine traffic on our networks, taking advantage of efficiencies in transport and collocation, among other items. MCI WorldCom's costs of entering the local market will be reduced because we will not need to duplicate certain sales, marketing, and administrative functions, and we will have reduced network costs resulting from the more rapid transfer of traffic to our local networks.

Duplicative capital expenditures for local network build out and information technology can be eliminated. Core sales, general, and administrative savings will be realized. These efficiencies

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[21] *Bell Atlantic/NYNEX,* at ¶ 139.

[22] Joint Reply at 11-12.

will create an opportunity for MCI WorldCom to become more engaged in local market opportunities than it could be if the two companies stood alone. Savings realized can be used to attack incumbent monopolists more aggressively.

E. Conclusion

GTE, BellSouth, and Bell Atlantic are not seeking to preserve and enhance local competition; they are seeking to prevent real local competition from ever getting started. It is in that context that their comments must be assessed. If the incumbent local exchange carriers really believed that the merger would reduce competition in local markets, their duty to shareholders would require them either to not participate in this proceeding or to support the merger. The incumbents' attacks speak volumes. The merger of MCI and WorldCom will serve to open local markets faster, and advances the Commission's public policy goal of promoting competition in all markets.

III. THE MERGER WILL NOT HARM, AND CAN ONLY ENHANCE, VIGOROUS COMPETITION IN THE INTEREXCHANGE MARKET

In the Joint Reply, MCI and WorldCom demonstrated that the merger would enhance vigorous competition in an already competitive market. Low entry barriers, sophisticated consumers, and other factors would foreclose any attempt after the merger to increase prices through tacit collusion. Moreover, the industry is becoming even more competitive as the number of significant facilities-based competitors grows. In the last twelve months, at least three carriers have started to construct, or announced plans to expand significantly, networks with nationwide coverage. These carriers will benefit from the decreasing unit cost of constructing new fiber networks to add significant competition to the market.

In addition, the BOCs, among others, are significant potential entrants once they satisfy the statutory criteria for entry into interLATA long distance. They have widely recognized brand names, a huge customer base, extensive facilities, administrative and technical resources, and massive financial resources.[23]

In the meantime, GTE attempts to convince the Commission that the long distance market is dominated indefinitely by AT&T, MCI, Sprint and WorldCom, with the first three colluding on price and only WorldCom offering real competition -- competition which, they say, will abruptly disappear after the merger. That picture does not correspond with reality or economically rational behavior.

In the first place, GTE now concedes, as it must, that there is increasing competition from

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[23] In its first quarterly report since acquiring NYNEX, Bell Atlantic reported revenues of over $7 billion. "Bell Atlantic Takes Charge of $1.5 Billion," *Wall Street Journal,* Oct. 23, 1997, at B2.

other carriers, including itself, and rates are declining for business customers. They argue only that some residential customers are still paying rates that are too high. Indeed, FCC Chairman William Kennard recently told an audience of consumer advocates, "Long distance rates fell 5.3% between January 1996 and November 1997. Long distances prices are now the lowest they have ever been."[24] Long distance carriers recently had an opportunity to review this history with the Commission at the invitation of the Chairman. In separate letters, AT&T, MCI and Sprint each reported that long distance rates were falling further and faster than access cost reduction -- evidence that competitive pressures, even in the residential market, are driving prices.[25] Significantly, a large portion of the reductions occurred in residential. A prime example is MCI's 5 Cent Sunday offering, available to all residential customers regardless of calling volume. Customers are clearly taking advantage of 5 Cent Sundays -- MCI's network now carriers more minutes each Sunday than we normally do on Mother's Day, the busiest calling day of the year.

With respect to large business purchasers, there is no doubt that carriers compete on price, quality, and innovation. Large business services are the most competitive of all, as evidenced by sophisticated customers who know how to adroitly play one provider off against another.

Moreover, in neither the business nor residential segment of the market is it appropriate to

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[24] FCC Chairman William Kennard to the National Association of State Utility Consumer Advocates, February 9, 1998.

[25] Letter from Jonathan B. Sallet, MCI, to FCC Chairman William Kennard, March 2, 1998 (citing long distance reductions in excess of access cost of $467 million); Mark C. Rosenblum, AT&T, to FCC Chairman William Kennard, March 5, 1998 (reductions in excess of access of almost $1 billion); and J. Richard Devlin, Sprint, to FCC Chairman William Kennard, March 4, 1998 (reductions in excess of access of $500 million). The analysis that each company used varied the time period over which the measurement occurred.

confine analysis to the largest interexchange carriers. Smaller long distance carriers presently have seized 16% of the market, up from 12% in 1996.[26] This growth rate is particularly impressive because these market shares grew in an expanding market. GTE opines that these competitors are not yet competitive. If that is true, how did they achieve such explosive growth? Market analysis that leaves these companies out ignores the real world.

In addition to the "other" interexchange competitors, an analysis limited to the largest carriers also ignores the several new nationwide interexchange networks that will be completed and become fully operational within the next two years. In the absence of any documentation, GTE proclaims that it will be years before these networks become competitive. That does not accord with those carriers' own representations or historical experience. Of course, potential competitors also include the Bell Companies, under the Commission's ruling in *Bell Atlantic/NYNEX*.[27]

Finally, GTE predicts that WorldCom, after the merger, will stop offering favorable wholesale discounts to resellers in some misguided effort to protect the MCI retail customers. That argument does not accord with the history of this market, as well as current industry practice, in which AT&T and MCI (as well as WorldCom itself) have competed extensively for both retail and wholesale services. Nor does it accord with common sense or economically rational behavior, except perhaps for a *de facto* monopoly company like GTE that *in fact* refuses to offer favorable discounts on local network capacity or services to local resellers. WorldCom's wholesale services

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[26] This statistic portrays the market share of companies other than AT&T, MCI, Sprint and WorldCom. Joint Reply at 30; Declaration of Robert E. Hall at ¶ 62, Attachment C to Joint Reply ("Hall Decl.")

[27] *See Bell Atlantic/NYNEX,* at ¶ 7.

have achieved explosive growth, and WorldCom fully intends to continue that growth. As stated in the Joint Reply, there is no basis to conclude that the merger adversely affects choices that resellers have, for a very simple reason -- the abundance of facilities-based competition means that facilities-based carriers either must offer services at wholesale rates or lose revenue to other facilities-based carriers.

In the following discussion, we present our detailed response to the points made by GTE and others under the four categories of analysis spelled out in the Commission's *Bell Atlantic/NYNEX* and *BT/MCI* decisions.

A. Relevant product and geographic markets

1. Wholesale and resale are not separate markets; and in any event, separate analysis does not change the result.

The product market must be defined as all interstate, domestic interexchange service, without further delineation. That is what the Commission did in the AT&T Non-Dominance Proceeding, where it adopted "a product market definitions of 'all interstate, domestic, interexchange services . . . with no relevant submarkets.'"[28] As the Commission noted, it had already used the same market definition in classifying AT&T's competitors as non-dominant.[29] Just last year, the Commission concluded that it will "treat [interexchange] services together, by analyzing aggregate data that encompasses all long distance services, rather than information particular to specific services." *LEC*

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[28] Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd 3271 (rel. Oct. 23, 1995), ¶ 22 (quoting *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefore,* CC Docket No. 79-252, Fourth Report and Order, 95 FCC2d 554, 564 (1983)).

[29] *Id.*

In-Region Interexchange Order, ¶ 43.[30]

We show at more length below that treating the retail and wholesale long-distance services as separate markets would, in any event, have no competitive consequence in the analysis of this merger. Wholesale service is a highly competitive business with multiple suppliers. It is growing more competitive with the entry of significant new carriers that have positioned themselves as carriers' carriers catering to IXC customers, and who do not have to establish brand name recognition to compete. The retail mass market is also competitive; and in any event, since WorldCom itself has no significant market share in that market, its merger with MCI will have no competitive consequence.

2. While there are different customer classes that can usefully be identified for long distance, there are no separate customer product markets.

In *BA-NYNEX*, the Commission identified three "customer groups" within the local exchange market: 1) residential and small business, 2) medium-sized business, and 3) large business/government.[31] As Professor Hall points out, the long-distance market is one in which supply-side substitutability blurs any distinctions between types of customers: "Because long-distance carriers who are currently active only in the business market are nonetheless capable of moving into the residential market, should higher prices in that market make the move attractive, the relevant market comprises both business and residential service." Hall Decl. ¶ 6.[32] However, it may

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[30] *LEC In-Region Interexchange Order.*

[31] *Bell Atlantic-NYNEX,* at ¶ 53.

[32] Prof. Hall also points out that "because many business long-distance calls are made from home, the distinction between residential and business is blurred to begin with." Hall Decl. ¶ 6.

be useful to evaluate the different segments of the long distance market separately to determine whether the merger raises any particular issues with respect to any segment. Applicants do take issue, however, with the Commission's three-part segmentation of the long distance market by customer groups. More reflective of today's long distance market is a two-part segmentation: (1) mass market products -- residential and small business; and (2) business products. There is no meaningful distinction between medium-sized business services and large business services for the purpose of selling long distance. Both are characterized by face-to-face customer service, the ability to use dedicated lines for some or all of their needs, and the likelihood that their service is provided via tariffed contract, as opposed to obtaining a service as defined in a generic tariff offering. Regardless of whether one analyzes these segments separately, the results remain the same -- competition for business customers is strong and would not be diminished due to the merger.

GTE argues that the large business/government group should be analyzed as a separate segment of the interexchange market because WorldCom is stronger in this segment than in the residential and small and medium-sized business segments. *GTE Comments* at 13-14. In its analysis, the Commission will examine whether there is "credible evidence suggesting that there is or could be a lack of competitive performance" with respect to large business or governmental customers.[33] We submit that no such evidence exists. These customers have considerable sophistication and experience in purchasing long distance service and dealing with long distance providers. As Professor Hall points out, a "business has the incentive to shop carefully and to extract the best possible deal from alternative sellers." Hall Decl. ¶ 88. As a result, as long as there are at

[33] *LEC In-Region Interexchange Order, supra* at ¶ 40.

least two carriers offering long-distance service, business buyers "have a chance at pushing the price all the way down from the monopoly level to the level of cost." *Id.*[34] In fact, as Professor Hall points out, "[t]oday, dozens of long-distance carriers offer bargains to businesses." *Id.* ¶ 89. There is no credible evidence of lack of competitive performance in the large business/government customer group.

It is noteworthy that, other than GTE, no business customers or association of business users have opposed this merger. And given GTE's other parochial reasons for opposing the merger, one may question whether a fear of losing its present wholesale contract with WorldCom is its real motivation.[35]

GTE argues that the "mass market" must be different from the business market and less competitive because customers do not take advantage of discounts and are receptive only to recognized brands. But the merger will have virtually no impact on this market because WorldCom, although providing wholesale services to carriers who do offer mass market products, has an insignificant market share of this retail segment. Accordingly, even if the mass market segment is analyzed separately and viewed as non-competitive, the merger would have no discernible impact because WorldCom has an insignificant market share.

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[34] GTE's own account of its participation in the wholesale market shows that it shopped carefully, procured competing bids, and obtained the best possible deal for itself. *See* Declaration of Debra Covey (attached to GTE's Petition to Deny) ¶¶ 3 and 4.

[35] GTE's existing wholesale contract with WorldCom gives it "multi-year" protection. Covey Decl. ¶ 3. In addition, as discussed at pp. 36-39, *infra*, GTE has obtained significant capacity on the Qwest network, which will shortly have nationwide coverage and become fully operational.

3. The long distance market is a national one.

The relevant geographic market must be defined as a single national market for long distance calling. That is the approach the Commission followed in the AT&T Non-Dominance Proceeding.[36] That was also the approach followed in the recent *Motorola-AMSC* decision, which states that "when a group of point-to-point markets exhibit sufficiently similar competitive characteristics (i.e. market structure), we may aggregate such markets, rather than examine each individual point-to point market separately."[37] There is no basis for a different approach here.

The Commission has stated that where "the competitive conditions for a particular service in any point-to-point market are sufficiently representative of the competitive conditions for that service in all other domestic point-to-point markets, then we will examine aggregate data, rather than data particular to each domestic point-to-point market."[38] Given the nationwide provisioning, marketing, pricing, sales and advertising of long distance services, as well as legal requirements that long-distance rates remain geographically averaged, there is no reason to follow a different approach here. Neither GTE nor any other party references any particular market in which separate analysis might make a difference. Presumably, GTE, as a competitor in the long distance market, would be

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[36] Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd 3271 (rel. Oct. 23, 1995), ¶ 22. As the Commission noted, it also followed the approach of defining a single national market in its proceedings classifying AT&T's competitors as non-dominant. *Id.*, citing *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefore,* CC Docket No. 79-252, Fourth Report and Order, 95 FCC2d 554, 573-75 (1983).

[37] *Application of Motorola, Inc., Transferor, and American Mobile Satellite Corporation, Transferee,* CWD No. 98-3, Memorandum Opinion and Order (rel. March 16, 1998), ¶ 29.

[38] *LEC In-Region Interexchange Order* ¶ 66.

aware of such evidence since it would be looking to exploit those opportunities.

GTE argues that market share information broken down by state or individual routes "is critical because resellers and smaller facilities-based carriers rely heavily on [WorldCom and MCI] to provide nationwide coverage, and other sources of supply may not be available on many routes." *GTE Comments* at 15. But that argument wrongly assumes that interexchange carriers can exploit local shortages, or localized absence of competition, to charge supracompetitive rates in some areas, while lowering rates in other areas where competition is present or there is no capacity shortage. This type of localized market situation does not -- and indeed, cannot -- exist in the case of interexchange services. Section 254(g) of the Act and this Commission's rules require interexchange carriers to provide interstate service to its customers in each State "at rates no higher than the rates charged to its subscribers in any other State." 47 C.F.R. § 64.1801(b).[39] And with respect to intrastate interexchange rates, once competition reaches any urban area within the State, the rate averaging requirement of Section 254(g) would prevent any interexchange carrier from charging customers in rural areas more than customers in urban areas where rates are competitive.[40] Neither GTE nor any other party has produced a shred of evidence that interexchange carriers have exploited local shortages or lack of competition to charge higher rates in discrete geographic areas. Indeed,

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[39] The Commission has exercised forbearance from enforcing section 254(g) as to temporary promotions, contract tariffs, Tariff 12 offerings, optional calling plans and private line services. However, temporary promotions are limited to 90 days; and contract tariffs, Tariff 12 offerings, and optional calling plans must be available to all similarly situated customers, regardless of their geographic location. Policy and Rules Concerning the Interstate, Interexchange Marketplace, Implementation of Section 254(g) of the Communications Act of 1934, as Amended, 11 FCC Rcd 9564 (rel. Aug. 7, 1996), ¶¶ 27, 29.

[40] *Id.* ¶ 46.

as Drs. Carlton and Sider point out, the industry practice exhibits uniformity in intrastate and wholesale rates, as well as interstate rates. Second Declaration of Dennis W. Carlton and Hal S. Sider, ¶¶ 24, 26. ("Second Carlton/Sider Decl.") The declaration is attached as Attachment C.

Moreover, some 75% of the U.S. population lives in LATAs served by six or more of the ten competitive networks that are presently in operation or will be within the two-year period of the Merger Guidelines, and 60% in LATAs served by eight or more of these carriers. Second Carlton/Sider Decl. ¶ 38. (The 10 networks are: AT&T, Sprint, MCI, WorldCom, Cable & Wireless, Qwest, IXC, Williams, LCI and Frontier. *Id.*) "Only 6 percent of the U.S. population live in areas in which the transaction would reduce the number of networks from four to three; 5 percent of the population live in areas in which the number of networks would fall from five to four, and 4 percent in areas in which a reduction from 6 to 5 would result." Second Carlton/Sider Decl. ¶ 39.

Moreover, several of these networks are shared by competitors, and "competition among independent owners of capacity provided by the same network could lead to more competition than competition between two geographically separated networks." Second Carlton/Sider Decl. ¶ 45. "This competition could be more intense than if the two firms each had non-overlapping networks." *Id.* Thus, even in areas where only a few networks are available, "failure to make an appropriate adjustment for multiple owners of network capacity will result in estimates of market shares and concentration that are biased upward." Second Carlton/Sider Decl. ¶ 43.

In short, there is no need for analysis of separate geographic markets, other than to delay this proceeding.

B. Actual, potential and precluded competitors

1. Significant actual competitors are not limited to the largest carriers.

GTE defines the significant actual competitors of MCI and WorldCom in the interexchange market to include only AT&T and Sprint. However, as pointed out in the Joint Reply, the "other" carriers category accounted for 12.1% of presubscribed lines as of the final quarter of 1996, and mushroomed to 16% by the third quarter of 1997. Joint Reply at 30-31; Hall Decl. ¶ 62. This category comprises over 600 competitors, at least 20 of whom have revenues over $100 million, and several of whom have revenues exceeding $1 billion, including LCI, Excel, Frontier, Cable & Wireless and GTE. Joint Reply at 30. As a group, this is the fastest growing segment of the industry, with annual growth rates *exceeding 40 percent. Id.* These carriers have proven quite adept at attracting and retaining interexchange customers.

GTE argues that the "other" category must be disregarded, because the "other" carriers allegedly do not have sufficient geographic coverage to provide effective competition, and because they face "a multitude of other barriers to entry that will take considerable time to overcome." Yet, most of these carriers, including LCI, Excel, Cable & Wireless and Frontier, are certified in virtually all states and have nationwide coverage. We have already pointed out that GTE's argument on geographic coverage ignores the geographic rate averaging requirement of the 1996 Act. Given the nationwide footprint of many of the "other" carriers," virtually all competing interexchange carriers will have to respond with competitive rates charged *nationwide,* since interexchange carriers cannot confine rate reductions to those areas where competitors are in operation, maintaining higher rates elsewhere. Nationwide pricing is, in fact, industry practice, and GTE fails to show otherwise. Second Carlton/Sider Decl. ¶ 24.

Moreover, GTE's argument overlooks the ability of networks to interconnect with each other, transcending the limitations of any particular network. As GTE well knows, every long-distance call utilizes more than just one network, if only for purposes of origination and termination. Total point-to-point coverage by a single network is not the norm in this market. As a totality, the competing long-distance networks have already achieved significant nationwide coverage, and that coverage is rapidly expanding.

We discuss in more detail below the relatively modest barriers to entry that the new entrants are facing. *See* pp. 37-41, *infra*. It suffices here to say that if carriers in the "other" category in fact "face a multitude of other barriers to entry that will take considerable time to overcome" (*GTE Comments* at 16-17), then how is it that this segment grew from a 12% market share in the final quarter of 1996 to 16% in the third quarter of 1997? GTE's long distance operations are a case in point. Since enactment of the Telecommunications Act in February, 1996, GTE has gained a market share of some 12% in its incumbent service territory.[41]

Finally, GTE argues that the "other" category should be disregarded because many of them are only resellers, purchasing capacity from the largest carriers. *GTE Comments* at 17-18. In fact, many of the "other carriers," such as Excel, Frontier, Cable & Wireless, and LCI, have become facilities-based carriers and are moving quickly to deploy nationwide networks, and scores of other resellers are securing regional and national network facilities as their traffic base increases. The recent announcement of a merger of LCI and Qwest illustrates the rapid evolution of resellers to major facilities-based carriers. Moreover, as the Commission has recognized, even pure resellers perform a significant competitive function, which becomes more significant as they acquire facilities

[41] John J. Keller, "GTE Net Falls 10% Due to Cost of Expansion," *Wall Street Journal*, Jan. 28, 1998, at B15.

and progress down the path to predominantly facilities-based service. Moreover, as new networks come on line within the next two years (*see* pp. 38-9, *infra*), the resellers will find additional sources of network capacity, and the migration of resellers to facilities-based carriers will likely accelerate.

In 1995, the "other" category of interexchange carriers (which then included WorldCom) accounted for 17.3 percent of interstate interexchange revenues.[42] At that time, in reclassifying AT&T as non-dominant despite its then 51% market share, the Commission found "unpersuasive the arguments that interexchange carriers other than AT&T, MCI and Sprint are too small to exert competitive pressure."[43] In this proceeding, the "other" category (without WorldCom) now accounts for 16% of the market. Hall Decl. ¶ 62. And given the accelerating rate of facilities ownership by "other" carriers, it seems likely that a larger portion of the "other carrier" competition is facilities-based than was the case in 1995, and will certainly be more so within the next two years as the Qwest, IXC, Williams and Level 3 networks become fully operational and the interexchange market continues to segment and differentiate. *See* pp. 38-9, *infra*. Moreover, the combined MCI WorldCom revenue share (as of the third quarter of 1997) will be 24 percent, not the 51 percent AT&T had in 1995. Hall Decl. ¶ 62. In this context, GTE's argument that the "other carriers" will not exert competitive price pressure is even weaker than the same argument which the Commission found "unpersuasive" in 1995 in the AT&T Non-Dominance Proceeding.

GTE's own market performance refutes its claim that only the four largest IXCs are significant. GTE itself is one of the "other competitors," and it must be regarded as significant in

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[42] Keller, *supra*, n.14.

[43] Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd 3271 (rel. Oct. 23, 1995), ¶ 62.

view of its spectacular growth (1.7 million customers and 12% of the long distance market in its service areas after two years of operation[44]) and its many competitive advantages: a large base of existing customers located in areas where only GTE can offer a package of local and long distance service (because of GTE's success in keeping out significant local competition despite the 1996 Act and the Commission's pro-competitive decisions); wide brand name recognition; and significant technical, administrative, marketing and financial resources.

In addition to GTE, other companies in the "other" category have experienced phenomenal growth rates.[45] Moreover, within this group there are several companies with over $1 billion annual revenues. In these circumstances, it would be highly artificial to designate only a limited number of these companies as "significant." If that were to be done, however, that designation would have to be given at least to the companies with over $1 billion in annual revenue -- a category that included, as of 1996, LCI, Excel, and Frontier, as well as GTE. Joint Reply at 30.

In addition, the so-called "other" carriers are competitively significant as a group. With 16% of the market and a 40% growth rate, they exercise significant pricing restraint and discipline on the market. "The combined effect of the hundred or so smaller carriers, each nibbling at the shares of the larger carriers, is to enforce a high level of competition in the market in general." Hall Decl. ¶ 69.

2. There are several significant potential competitors.

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[44] Keller, *supra*, n.41.

[45] As described in the Joint Reply, the operating revenue of Var-Tec Telecom grew from virtually zero in 1993 to $470 million in 1996, while LCI's operating revenues grew from $317 million in 1993 to over $1.1 billion in 1996. Joint Reply at 39.

Qwest is a significant potential interexchange competitor because its network, which is scheduled for completion in the second quarter of 1999, will serve more than 125 cities representing approximately 80% of the data and voice traffic originating in the United States.[46] In addition, once its recently-announced merger with LCI is consummated, Qwest will have over two million business and residential customers.[47] The largest facilities-based carriers will face significant price competition for most of their business *from this single source.*

GTE argues that the new networks that will be built and operational within the next two years, plus the competitors in the "other" category, should be disregarded because only the largest facilities-based carriers have POPs in a sufficient number of LATAs to achieve coverage of a significant percentage of the U.S. population. Without a POP in the LATA, GTE argues, a competitor must pay additional transport charges, making it unable to undercut oligopolistic pricing by the larger carriers. *GTE Comments* at 23-26.

We have previously pointed out that this argument ignores the geographic averaging requirement of Section 254(g) of the 1996 Act, which will prevent long distance carriers from charging competitive interstate rates in areas where competitors operate while charging higher rates in non-competitive areas, as well as the industry practice of uniformity for intrastate as well as interstate rates. Second Carlton/Sider Decl. ¶ 24-26.[48] GTE's argument also ignores the fact that

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[46] Dow Jones News/Retrieval Business and Finance Report, March 9, 1998.

[47] *Id.*

[48] GTE also ignores the fact that start-up IXCs may employ Feature Group A for interexchange traffic in areas where they do not have a POP. This is exactly how MCI broke into the IXC market in the early 1980's.

75% of the population live in areas that will be served by six or more networks, and that even in the remainder of the country competing providers sharing a single network will compete head-to-head, bringing significant consumer benefits. Second Carlton/Sider Decl. ¶¶ 38, 45.

Competing providers of significant long-distance capacity that will be ready within the next two years include Qwest Communications, IXC, Williams Co. and Level 3. Communications. *See* Joint Reply at 35-36, Second Carlton/Sider Decl. ¶¶ 14-16.[49] Williams, which previously announced an investment of $2.7 billion for construction of a 32,000 route-mile national fiber optic network, recently announced plans to accelerate the deployment of its network. Second Carlton/Sider Decl. ¶ 114. Drs. Carlton and Sider point out that "[a]s a group, Qwest, IXC, Williams and Level 3 alone are planning to deploy 72,000 fiber route miles of high capacity fiber and electronics, nearly double AT&T's current route mileage (and probably significantly more than double AT&T's fiber miles, due to the large number of fiber strands per cable being deployed by new networks)." Second Carlton/Sider Decl. ¶ 16. This is capacity that will be operational well within the two-year period prescribed by the Merger Guidelines. It will not have to await any ramp up of procedures and back office facilities. If any network lacks the necessary facilities to terminate the traffic, it can deal with resellers who do or make other arrangements; indeed, every long-distance network uses other carriers to some extent to terminate its traffic.

Also included among competitors must be Frontier and GTE (to whom Qwest has sold significant portions of its network), as well as LCI, Vyvx, Inc., DTI, Consolidated Communications Telecom Services, and GST -- to whom IXC has sold capacity. Joint Reply at 36. In addition,

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[49] Entry that is likely to occur within two years is viewed as counteracting a merger's effect on competition. *Bell Atlantic-NYNEX,* at ¶ 130.

Alliant Communications has recently expanded its fiber optic network and formed a consortium of regional networks. Declaration of Dennis W. Carlton and Hal S. Sider, Attachment B to Joint Reply, at ¶ 43 ("First Carlton/Sider Decl.")

GTE also totally ignores the Regional Bell Companies, which are significant precluded competitors. They are clearly planning a major effort in the long-distance market once they obtain Section 271 authority; they could hardly do otherwise in light of the success achieved by GTE and SNET. The Commission has stated that in defining the relevant markets, it will consider "not just the markets as they exist today, but as we expect they will exist after a Bell Company receives authorization to provide in-region interLATA services pursuant to Section 271 of the Communications Act."[50] That ruling should be followed here, and the Bells counted as potential entrants, since it is entirely within their power to satisfy the terms of Section 271.

C. Barriers to entry or expansion.

1. Barriers to entry or expansion are not sufficient to deter significant new competition within the next two years.

The barriers to entry or expansion for interexchange services are not significant, for several reasons. First, to spread the initial capital costs of building a national network, new competitors may follow a strategy of initial entry through resale, followed by increasing investment in switching and transmission capacity based on marketing success; this has been the strategy followed by a number of successful entrants in recent years, including WorldCom, LCI, VarTech Telecom, and MCI. Joint Reply at 39.

Second, new entrants seeking to own transmission capacity may lease or purchase shares of

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[50] *Bell Atlantic/NYNEX,* at ¶ 7.

existing networks or networks under construction, thus spreading the capital cost. This strategy has also been followed by a number of new entrants, such as Frontier. Joint Reply at 35-37. Qwest's experience is illustrative. It recently estimated that its construction of a national 16,000 route mile SONET four-ring fiber optic telecommunications network will cost $2.4 billion, including necessary electronics and five switches.[51] Qwest has already obtained approximately $1.1 billion in dark fiber contracts from Frontier, GTE, WorldCom and others.

Third, rapid improvements in technology enable new and existing competitors to increase exponentially the amount of traffic that a single strand of fiber can carry, allowing rapid expansion of network capacity without additional network construction. Joint Reply at 37. Moreover, while the costs of building a new network are substantial, several companies have recently undertaken this task, demonstrating that the capital is available. Joint Reply at 34-37.

2. GTE has greatly exaggerated the barriers to entry and expansion.

GTE argues that there are several barriers to entry which will prevent the new networks being built by Qwest, IXC, Level 3 and Williams from providing significant competition within the next two years, even though they will be operational within that time frame. *GTE Comments* at 21-32.

This argument is inconsistent with the recent history of this market, in which several small competitors have quickly become major players in much less than the five-year time frame that GTE describes as being necessary.

GTE lumps together barriers to entry to the retail as well as the wholesale market (although elsewhere it fervently insists that the markets are separate). Thus, GTE argues that an entrant into

[51] Qwest SEC Form S4, Dec. 22, 1997, p. 9.

the retail market must "develop a strong brand name in the face of incessant advertising by the incumbents." *GTE Comments* at 22.[52] But networks selling capacity to resellers do not face this barrier. Indeed, they can sell capacity to GTE (as the Qwest network has already done) or possibly to the RBOCs (once they satisfy the requisite statutory criteria to gain Section 271 approval), who can then reach the retail market on the basis of their own brand name.

In terms of when a new network can become an effective competitor once it is built and in operation (as the Qwest, Level 3, IXC and Williams networks will be shortly), GTE presents a grossly exaggerated picture of the difficulties involved. GTE overlooks the cost advantages that newer technologies give to recently-constructed fiber networks.[53]

In addition, GTE overlooks the ability of a new network (such as Qwest's) to get to market by selling capacity to resellers who already have switches, OSS and other support systems. For example, when Qwest sells capacity to GTE, it is selling to an established organization which already has the support systems needed. Portions of the Qwest network are already operational, some two years after Qwest started construction.[54] GTE's description of a five-year time-frame for getting to market is simply not borne out by the facts.

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[52] GTE's emphasis on the necessity for mass advertising is contradicted by the experience of dial-a-round carriers like Telco and Vartec, who have achieved considerable market success with virtually no brand recognition.

[53] Qwest states that its "advanced fiber and transmission electronics are expected to provide the Company with lower installation, operating and maintenance costs than older fiber systems generally in commercial use today." Qwest Communications International, Inc., SEC Form 10-Q for quarter ended September 30, 1997, at 19. Its network, which it commenced constructing in 1996, is already being utilized to provide dedicated line and switched access service. *Id.* at 15, 19-21.

[54] Qwest SEC Form 10-Q, Sept. 30, 1997, at 19.

GTE further argues that a new network cannot become an effective competitor until it achieves virtually ubiquitous geographic coverage. Also, GTE argues, it must acquire its own POPs in all or virtually all LATAs, or face the competitive disadvantage of incurring additional transport charges which will make its rates uncompetitive. *GTE Comments* at 23-26. However, as WorldCom's own experience demonstrates, a competitive network can impose competitive discipline nationwide simply by being competitive in significant metropolitan areas. That is because there is significant facilities-based competition nationwide. GTE and other IXCs are buying capacity at cost-based rates to go where their networks do not go. Further, the nationwide geographic averaging requirement of section 254(g) precludes interexchange carriers from selectively lowering their rates only in those areas where they encounter significant competition. Indeed, GTE concedes that WorldCom itself does not have POPs in some 90 of the nearly 200 LATAs, and yet is a significant competitor. *GTE Comments* at 24. It is simply not the case that ubiquitous geographical and POPs coverage is necessary before a carrier becomes a significant competitor.

Moreover, as pointed out by Drs. Carlton and Sider, the Qwest network will have POPs covering 78% of the nation's population, while the Williams and IXC networks will have POP coverage of 72% and 61% of the population respectively. Second Carlton/Sider Decl. ¶¶ 21. There is no principle of economics or common sense to support GTE's argument that WorldCom's 82% population coverage is "significant" and qualifies it for membership in the so-called "Big Four," while competing networks with coverage ranging from 61% to 78% are competitively insignificant. As Drs. Carlton and Sider point out, the new networks "will soon have a presence at least as significant as WorldCom's as recently as two years ago." Second Carlton/Sider Decl. ¶ 34.[55]

GTE argues that for "several years," new entrants will be unable to achieve economies of scale that apply to the "Big Four." *GTE Comments* at 26. But the Qwest network is already in operation. And GTE itself, in its May, 1997 announcement of its purchase of a portion of that network, stated that the network would be "fully operational next year" and will enable GTE "to reach virtually the entire U.S. population." GTE's operational personnel apparently do not have the apprehensions that its lawyers describe.[56]

Finally, GTE argues that there is a shortage of qualified network engineers and telecommunications software developers, and that new entrants will face high and increasing labor costs. *GTE Comments* at 30. The argument makes no sense. To the extent that new entrants bid up the compensation of new technical employees (and attract employees from the incumbents in the process), that raises the cost of technical help for all market participants, including the incumbents. When all participants face the same labor market there is no competitive advantage or disadvantage stemming this factor.

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[55] "WorldCom had only about 110 POPs as recently as 1996. In contrast, by next year, IXC is expected to have deployed 106 POPs, and Qwest is expected to have deployed 125." Second Carlton/Sider Decl. ¶ 34.

[56] On May 6, 1997, GTE announced a series of transactions to "position GTE to have the fastest, most reliable and most secure national network available, enabling end-to-end managed network solutions that we believe will be unmatched in the industry." GTE explained that this network, which it is purchasing from Qwest Communications, would be "fully operational next year" and that "[a]t that point, we will be in a position to reach virtually the entire U.S. population." "GTE Announces Initiatives to Become a Leading National Provider of Telecommunications Services -- Will Acquire BBN in Transaction Valued at $616 Million -- Purchases Fiber-Optic Network From Qwest -- Creates a New National Sales Service and Marketing Company" available at <http://www.gte.com/g/news/050697.html> (visited March 19, 1998).